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In the Supreme Court of the United States

OCTOBER TERM, 1996

INDICATED EXPANSION SHIPPERS, PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

WALTER DELLINGER
Acting Solicitor General
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

SUSAN TOMASKY
General Counsel
JOSEPH S. DAVIES
Acting Solicitor
TIMM L. ABENDROTH
Attorney
Federal Energy Regulatory Commission
Washington, D.C. 20426

14 pp

QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission (FERC) can take into account the impact on matters within its jurisdiction of state regulation that, under the Hinshaw Amendment to the Natural Gas Act, 15 U.S.C. 717(c), is otherwise a matter of exclusive state jurisdiction.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-17) is reported at 92 F.3d 1239. The opinions of the Federal Energy Regulatory Commission (Pet. App. 19-303) are reported at 54 F.E.R.C. (CCH) ¶ 61,035, 56 F.E.R.C. (CCH) ¶ 61,192, 57 F.E.R.C. (CCH) ¶ 61,097, and 62 F.E.R.C. (CCH) ¶ 61,243.

JURISDICTION

The judgment of the court of appeals was entered on August 23, 1996. Petitions for rehearing were denied on October 24, 1996. Pet. App. 305-306. The petition for a writ of certiorari was filed on January 22, 1997.

The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

This case involves a condition placed by the Federal Energy Regulatory Commission (FERC) on a certificate of public convenience and necessity that FERC granted under Section 7(e) of the Natural Gas Act (NGA), 15 U.S.C. 717f(e). The certificate authorized Pacific Gas Transmission Company (PGT) to expand its pipeline facilities for transporting gas from Canada to Malin, Oregon, at the California border. Because FERC concluded that rates and conditions on the use of PGT's pipeline expansion discriminated against interstate shippers, FERC imposed a condition on the certificate until PGT could demonstrate that it no longer discriminated. The court of appeals invalidated that condition. Petitioners are some of the interstate gas shippers that intended to use PGT's expansion facilities, but that opposed what they viewed as discriminatory practices impairing their competitive position.

1. PGT's pipeline connects at Malin to the facilities of PGT's parent company, Pacific Gas & Electric Company (PG&E). Pet. App. 4. Whereas PGT's pipeline runs interstate and thus is subject to the Natural Gas Act, PG&E's facilities are entirely within the State of California, and thus are regulated by the California Public Utilities Commission (CPUC) pursuant to the Hinshaw Amendment to the NGA, 15 U.S.C. 717(c). The Hinshaw Amendment exempts from the NGA those companies that, like PG&E, receive gas within or at the boundary of a State if all

the gas is consumed within the State and subject to state commission regulation.[1]

Pursuant to its authority under the Hinshaw Amendment, the CPUC authorized PG&E to expand its facilities in California in order to receive the additional gas from PGT's expansion for distribution in California. PGT then placed a condition on shippers seeking to use its proposed interstate pipeline expansion, requiring them contractually to commit also to use PG&E's proposed expansion facilities in California. Petitioners believed that requirement would make it uneconomical for them to sell gas in California in competition with PG&E. Pet. App. 4-6.

2. Before FERC granted PGT's certificate, petitioners opposed PGT's application, contending that PGT's contractual requirement that they use

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[1] Section 717(c) states:

> The provisions of this chapter shall not apply to any person engaged in or legally authorized to engage in the transportation in interstate commerce or the sale in interstate commerce for resale, of natural gas received by such person from another person within or at the boundary of a State if all the natural gas so received is ultimately consumed within such State, or to any facilities used by such person for such transportation or sale, provided that the rates and service of such person and facilities be subject to regulation by a State commission. The matters exempted from the provisions of this chapter by this subsection are declared to be matters primarily of local concern and subject to regulation by the several States. A certification from such State commission to the [Federal Energy Regulatory] Commission that such State commission has regulatory jurisdiction over rates and service of such person and facilities and is exercising such jurisdiction shall constitute conclusive evidence of such regulatory power or jurisdiction.

PG&E's planned, expensive expansion facilities in California constituted an illegal "tie-in." On August 1, 1991, FERC issued a certificate authorizing PGT's expansion under Section 7(e) of the NGA, 15 U.S.C. 717f(e), subject to the condition, *inter alia*, that PGT modify its contracts with petitioners to eliminate the tie-in. Pet. App. 88-234.

3. After PGT complied with FERC's condition, the CPUC issued orders with respect to PG&E that had the same tie-in effect. Those orders required petitioners to use PG&E's expensive expansion facilities before they could "cross over" to PG&E's pre-existing, lower-priced facilities. They also imposed a "postage stamp" rate structure (*i.e.*, one employing flat rates that did not vary with distance) that effectively required petitioners to pay PG&E as much for transportation of gas to customers in Northern California, just across the border from the terminus of PGT's interstate pipeline at Malin, Oregon, as they would have paid for transportation to Southern California. See Pet. App. 203-211.

4. On October 24, 1991, FERC modified its August 1 order in response to additional demand for gas that had arisen in California. Pet. App. 64-85. In lieu of its earlier requirement that the tie-in be eliminated before PGT could go forward with construction, FERC authorized the construction to proceed, but reduced PGT's rate of return on equity on its expansion facilities from 12.50 to 10.13% until such time as PGT demonstrated that neither its rates and practices nor those of PG&E "result in unduly discriminatory restraints on shippers' access to transportation on PGT's expansion project and transportation service within California." *Id.* at 84.

Petitioners and other parties sought rehearing before FERC, arguing that the rate-of-return condition would not be effective in eliminating the discrimination, and that FERC should not have authorized construction under those circumstances. Pet. App. 57. In its order on rehearing, FERC adhered to its decision, explaining that it "consider[ed] PGT's reduced rate of return * * * [a] condition reasonably tailored to accomplish [FERC's] goal of inducing a change to a policy beyond [FERC's] jurisdictional purview." *Id.* at 60. FERC stated it would not "dictate the form a remedy might take" that would lead it to lift the rate-of-return condition it imposed on PGT, because "the unduly discriminatory rate conditions are the product of rate and transportation policies subject to the jurisdiction of the CPUC." *Id.* at 58.

5. On appeal, PGT and the CPUC argued that FERC exceeded its jurisdiction in imposing the rate-of-return condition on PGT in order to influence regulatory authority reserved to the State under the Hinshaw Amendment. Petitioners and others supported FERC's exercise of jurisdiction, but argued that the PGT/PG&E arrangement that the CPUC sanctioned was unduly discriminatory and the rate-of-return condition would be ineffective to remedy the discrimination. See Pet. App. 4.

The court granted PGT's petition for review and denied those of the expansion shippers (petitioners in this Court).[2] The court of appeals held that FERC

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[2] Before the court of appeals entered its judgment, PGT entered into a settlement with certain of its customers, including the petitioners in this case (with the exception of Chevron U.S.A.). The settlement established rates PGT would be permitted to charge under new rate schedules proposed by PGT to replace the schedules FERC approved. Pursuant to

could not use its Section 7(e) authority under the NGA, 15 U.S.C. 717f(e), to condition the certificate it issued to PGT for the purpose of inducing PGT to pressure the CPUC to change the rate design authorized for PG&E. The court identified the "pivotal question" as "whether the Commission may exercise its power over an interstate pipeline in a manner intended to influence a state agency's regulation of a Hinshaw pipeline." Pet. App. 15. The court held that FERC could not exercise its Section 7(e) certificate power as it had in this case:

> The Commission lowered PGT's return on equity specifically and only to "induc[e] a change to a policy beyond [its] jurisdictional purview," *i.e.*, to pressure the CPUC to regulate PG&E as the Commission desired but could not itself require. Under the circumstances, the Com-

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the settlement, the customers agreed not to oppose elimination of the 10.13% rate-of-return condition FERC had imposed on PGT. PGT in turn agreed that, if it prevailed in the pending appeal, it would not assess the customers for the revenues it lost due to the 10.13% rate-of-return ceiling. Following the court of appeals' decision, FERC approved the settlement, imposing it as a decision on the merits as to the customers who had protested it. *Pacific Gas Transmission Co.*, 76 F.E.R.C. (CCH) ¶ 61,246, at 62,273-62,274 & n.69 (Sept. 11, 1996); see 18 C.F.R. 385.602(h)(1)(i) (authorization for imposition of settlement). Petitions for rehearing of FERC's order approving the settlement are pending. The existence of the settlement, FERC's order approving it, and the pending proceedings concerning that order are additional reasons to deny certiorari here.

> mission was indeed attempting to do indirectly what it could not do directly.

Id. at 16. The court observed that, "[g]iven a proper evidentiary record," FERC could have "avoided any Hinshaw restraint on its jurisdiction by concluding that PGT and PG&E undertook this project as a single company." *Id.* at 12. The court noted, however, "that the Commission did not reach this conclusion," and the court therefore treated PGT and PG&E "as distinct companies, as did the Commission." *Ibid.*

ARGUMENT

We read the court of appeals' decision more narrowly than do petitioners, and thus do not believe that certiorari is warranted. Although petitioners themselves "agree with the Circuit Court's conclusion that FERC may not adopt a remedy with the intent to 'influence a state agency's regulation of a Hinshaw pipeline'" (Pet. 20 (quoting Pet. App. 15)), they characterize the decision below as broadly preventing FERC from exercising regulatory authority in other ways that affect Hinshaw pipelines, see, *e.g.*, Pet. 10, 11. Contrary to petitioners' contention, the court did not categorically preclude FERC from considering matters beyond its jurisdiction if they affect jurisdictional sales or transportation. The court of appeals' decision does not conflict with any decision of any other court of appeals or of this Court, and does not present an important or recurring issue. Review is therefore unwarranted.

1. Petitioners misread the court of appeals' decision when they contend that it "inverts" preemption doctrine and "renders FERC powerless to protect interstate shippers of gas from unduly discriminatory and anticompetitive conditions if those conditions are

imposed by a State agency in the guise of 'rate policies' regarding a Hinshaw pipeline." Pet. 9; see also Pet. 16. Neither the court of appeals nor FERC held that FERC could not have alleviated the precise discrimination posed by the CPUC's action by, for example, treating PGT and PG&E as a single entity, or by exercising federal statutory authority in a manner that would preempt contrary state law. Petitioners themselves acknowledge that the court of appeals "did not reach the issues raised by [petitioners]," Pet. 6, and that the court recognized that FERC might have "avoided any Hinshaw constraint upon its jurisdiction by concluding that PGT and PG&E undertook this project as a single company," Pet. 15 n.8 (quoting Pet. App. 12).

As the court of appeals pointed out (Pet. App. 10-12), in circumstances in which the record shows that Hinshaw status is used to subvert FERC's jurisdiction over interstate transportation and obtain an unfair competitive advantage, FERC may "disregard the separate corporate status of entities that would otherwise be considered nonjurisdictional." *Id.* at 12 (citing *KansOk Partnership*, 73 F.E.R.C. (CCH) ¶ 61,160, at 61,484 (Nov. 2, 1995); *Louisiana Gas Sys. Inc.*, 73 F.E.R.C. (CCH) ¶ 61,161 (Nov. 2, 1995)). Indeed, since the court of appeals' decision in this case, the Commission has exercised its authority under federal law to invalidate certain charges assessed by a local distribution company regulated by the CPUC. *Union Pac. Fuels, Inc.* v. *Southern California Gas Co.*, 76 F.E.R.C. (CCH) ¶ 61,300 (Sept. 19, 1996), reh'g denied, 77 F.E.R.C. (CCH) ¶ 61,283 (Dec. 19, 1996), petition for review pending *sub nom. Public Util. Comm'n of California* v. *FERC*, No. 97-1028 (D.C. Cir. filed Jan. 14, 1997). In sum, contrary to

petitioners' contentions, the court of appeals' decision merely precludes FERC from using its authority for the purpose of pressuring interstate pipelines to influence state regulation of intrastate activities; it does not circumscribe FERC's exercise of its remedial authority in other ways.

2. Petitioners mistakenly claim (Pet. 14-21) that the court of appeals held that FERC may not exercise its authority under the Natural Gas Act in a manner that preempts state regulatory efforts. FERC never invoked its preemptive authority here, and the court below did not reach that issue. Petitioners therefore err in asserting (Pet. 15) that this case is in conflict with *United Distribution Cos.* v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996), petitions for cert. pending, Nos. 96-1186, 96-1187, 96-1188 & 96-1189 (filed Jan. 27, 1997). In *United Distribution*, the District of Columbia Circuit upheld FERC's preemption of state regulation over buy-sell transactions where FERC had found that state regulation interfered with its authority to regulate interstate transportation. *Id.* at 1156-1157.[3] The court of appeals upheld the FERC order establishing a uniform capacity-reallocation program against a claim that, to the extent that it applied to capacity held by local distribution companies, the order violated the Hinshaw Amendment. As the court of appeals explained, "the Commission's authority to regulate capacity release arises from its jurisdiction

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[3] As the court explained in *United Distribution*, 88 F.3d at 1154-1155, buy-sell transactions occur when an end user of gas purchases gas at a point of production, and a local distribution company (LDC) that services the end user transports the gas first under its own transportation rights on an interstate pipeline and later across its local distribution facilities to the end user.

over the interstate pipeline that consummates the transaction and the subject of the transaction, the interstate transportation of gas, entirely independent of its jurisdiction over the releasing or replacement shipper." *Id.* at 1153 n.62 (as amended Oct. 29, 1996 (amendment order reprinted in Appendix B to Pacific Gas Transmission Co. Br. in Opp.)). The situation here, where FERC never invoked its preemptive power, is not analogous to the situation in *United Distribution*.

3. Petitioners misconstrue the opinion of the court of appeals when they state that "FERC is stripped of its ability to even consider the consequences [of state regulation] on interstate shippers of natural gas simply by virtue of the source of those consequences," and that the upshot of the court's opinion "is that the Hinshaw exemption is so exclusively insulative that a Hinshaw pipeline and/or its state regulatory body could promulgate any variety of policies antithetical to the rights of interstate shippers." Pet. 9. Petitioners take out of context a sentence in the opinion's concluding paragraphs stating that this case involves "an express congressional reservation of jurisdiction to another body," which "places the matter off limits to the FERC." Pet. 8-9. Read together with the court's acknowledgement (Pet. App. 12) that FERC could have treated PGT and PG&E as a single entity and thus subjected the overall arrangement to federal regulatory authority, the court's statement is correctly understood as limited to the circumstances of this case, in which FERC sought to induce an interstate pipeline to seek to influence the State to reverse its regulatory action. Indeed, in the sentence preceding that statement, the court acknowledged that "the Commission

ordinarily has the authority to consider a matter beyond its jurisdiction if it affects jurisdictional sales." *Id.* at 17. The language upon which petitioners rely refers only to a situation in which FERC used its authority over the rates of an interstate pipeline in order "to induc[e] a change [of state] policy," *id.* at 60—action that petitioners agree the agency may not take. Pet. 13 n.4.[4]

CONCLUSION

The petition for writ of certiorari should be denied.

Respectfully submitted.

WALTER DELLINGER
Acting Solicitor General

SUSAN TOMASKY
General Counsel

JOSEPH S. DAVIES
Acting Solicitor

TIMM L. ABENDROTH
Attorney
Federal Energy Regulatory Commission

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[4] Petitioners seek support (Pet. 10-13) for their position in the manner in which the court of appeals distinguished this case from *FPC* v. *Conway Corp.*, 426 U.S. 271 (1976), and *FPC* v. *Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1 (1961). Contrary to petitioners' contentions, however, the court of appeals did not read those decisions categorically to bar FERC from exercising its remedial authority in a way that may affect sales or transportation under state regulatory jurisdiction. Rather, the court reasoned that those decisions did not support FERC's effort indirectly to change state rate policies by pressuring an interstate pipeline through a reduction of its rates. See Pet. App. 14-16.